STATE OF WASHINGTON

OFFICE OF FINANCIAL MANAGEMENT

Insurance Building, PO Box 43113 • Olympia, Washington 98504-3113 • (360) 902-0555

August 12, 2013 ***Sent via email only: August 12, 2013***

TO: Greg Devereux, Executive Director
Washington Federation of State Employees

FROM: Rick Hall, Assistant Director
OFM/Labor Relations Division

RE: **ESSB 5931 – Review of Department of Enterprise Services: Mail Delivery Services**

As you know, ESSB 5931 directed the Office of Financial Management to conduct a review of the programs and services performed by the Department of Enterprise Services (DES) to determine whether a program or service may be performed by the private sector in a more cost-efficient and effective manner than being performed by the department. Attached please find a memo from David Schumacher to Chris Liu at DES outlining the completed study for mail delivery services outside of Thurston County. In this memo, DES is directed to not move forward at this time with contracting for mail delivery services outside of Thurston County.

If you have any questions, please contact Franklin Plaistowe at (360) 725-5166.

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TO: Chris Liu, Director
Department of Enterprise Services

FROM: David Schumacher
Director

SUBJECT: OFM DETERMINATION ON MAIL DELIVERY SERVICES OUTSIDE THURSTON COUNTY

Pursuant to Section 104(5) of Engrossed Substitute Senate Bill 5931, I am writing to inform you that the Office of Financial Management (OFM) has determined through the requests for proposals issued by DES that mail delivery services outside Thurston County cannot be provided at a reduced cost and with greater efficiency by the private sector. Therefore, DES may not enter into contracts for these services. This memorandum reviews the background of the service and provides our analysis of why the state would not benefit from a private market contract for mail delivery services outside Thurston County.

As you know, ESSB 5931 directed the Office of Financial Management to conduct a review of the programs and services performed by the Department of Enterprise Services (DES) to determine whether a program or service may be performed by the private sector in a more cost-efficient and effective manner than being performed by the department. Up to six activities and services may be selected by OFM each biennium under this review. In conducting its review, OFM is authorized to break programs down into discrete services or activities or the programs may be reviewed as a whole. However, priority for selection shall be given to agency activities or services that are significant, ongoing functions.

For the 2011-13 biennium, OFM selected for review:

- Bulk print (required by ESSB 5931)
- Mail delivery services outside Thurston County
- Website design and maintenance services, including internet portal and e-Government services

For each of the selected activities, DES must conduct a procurement process. If OFM determines through the procurement process that the activity or service could be provided by the private sector at a reduced cost and with greater efficiency, DES may proceed with the contract.

For more information on ESSB 5931, go to:
http://apps.leg.wa.gov/billinfo/summary.aspx?bill=5931&year=2011.

Background

In 1990, the Efficiency Commission conducted a study of state mail operations. The study found redundancy in agency mail operations and under-utilization of agency mail processing equipment. The Efficiency Commission recommended consolidating state agency mail operations. During this same time period, Washington state government was assigned by the United States Postal Service (USPS) the unique zip code of 98504 for its Thurston County mail delivery. USPS regulations require customers with a unique zip code to receive all of their mail in bulk without prior sorting or separation by USPS. The USPS delayed implementation of this regulation for Washington state government, recognizing that the 1991 supplemental operating budget contained funds to implement a Consolidated Mail Service (CMS) program. CMS began operations in 1992.

Since that time, CMS sorts and delivers incoming federal mail addressed to state agencies using the 98504 zip code. In an effort to utilize an economy of scale, CMS also established delivery routes outside Thurston County to extend CMS' outbound discount and low-cost interagency processing to more locations. CMS currently operates seven routes outside Thurston County requiring seven full-time equivalent employees.

Processing of all incoming and outgoing mail (both USPS and interagency delivery) occurs at the CMS Central Terminal in Olympia. CMS presorts the mail daily for drop-off at each location on each route outside Thurston County. Items picked up along the route are returned to CMS for processing. However, there are frequent inter-route deliveries that are handled by the route driver without CMS processing.

A CMS survey estimates there are 778,000 interagency pouches[1] being delivered on the routes outside Thurston County each year. In addition, the survey predicted there could be nearly 300,000 pouches collected outside of Thurston County for delivery in town. In total, this amounts to approximately a million deliveries per year.

DES Request for Proposal (RFP)

On October 8, 2012, DES issued a request for proposal for performance of mail delivery at locations outside Thurston County currently served by seven state delivery routes, beginning and ending at the CMS facility. Vendors were required to:

- Comply with all applicable state and federal regulations, including but not limited to, the Private Express Statutes (PES) and Federal Regulations Title 39 parts 310 and 320
- Comply with all privacy regulations
- Wear recognizable uniforms
- Load the designated freight
- Pick up and deliver along each route
- Maintain the chain of custody without inter-mixing state with other materials
- Maintain a staff of qualified drivers

[1] Pouches are string-fastened, flap-topped, reusable sleeves holding flat 8" by 11" material. Contents of each pouch usually relate to a single topic, but may be a few sheets up to a 1" thick manual.

Vendors were allowed to propose serving all locations on all seven state delivery routes. Alternatively, vendors could propose serving all locations on one or more state delivery routes. Vendors who propose to serve more than one state delivery route, but not all seven, were allowed to combine or redefine routes; however, all locations within the chosen state delivery route(s) must be served. This requirement was included to avoid cherry-picking of locations, which if allowed, could increase DES costs or result in a current location being unserved.

The RFP required the vendor to be responsible for maintaining schedules as agreed, ensuring staff performance levels, and providing ongoing driver training. This vendor also required to have sufficient capital and resources to accomplish the services described herein. DES would accept proposals that include subcontractors only if the vendor submitting the proposal agrees to take complete responsibility for all actions of their subcontractors. Vendors were required to state whether subcontractors would or would not be used.

Vendors were required to submit pricing for each route to be billed monthly to the state. Vendors supplied an annual total and monthly total price amount inclusive of all costs associated with performing the service for each route included in its proposal. If an alternate route was offered, the vendors were required to supply a rate that is inclusive of all costs associated with performing the alternate route and describe how they arrived at the rate proposed.

The Apparent Successful Vendor (ASV) was expected to assume the role of current delivery services and have the capability of assuming similar activity now being performed. In addition, the ASV was expected to negotiate in good faith a performance-based contract with DES to ensure clear expectations for both parties and further definition of roles and responsibilities for successful service outcomes. A contract awarded under the RFP would be negotiated for an initial term of two years with an opportunity for extensions not to exceed a total of eight years.

The full content of the RFP can be found at:
http://www.ofm.wa.gov/reports/mailServicesOutsideThurstonCounty_RFP.pdf.

The RFP asked vendors to answer a series of questions in five categories: (1) an introductory overview demonstrating that the vendor meets the RFP's minimum qualifications (2) a management proposal outlining their organization, experience and proposed business plan, (3) a technical proposal defining the routes for proposed service and fleet, (4) references, and (5) proposed price. DES weighted the scores so that a vendor's introductory overview was a pass/fail determination. Vendors with a pass evaluation were then scored on the remaining categories with a price worth 45 points of the score, management and technical proposal each were worth 25 points, and references were worth 5 points of the score.

Two vendors submitted proposals – BeavEx and Delivery Express. Both are organized as centralized service cores using subcontractor-drivers. The core business provides the back office support, marketing, contracting, dispatch and oversight. They employ subcontractor-drivers to make the deliveries. Each subcontractor-driver is a private business with its own vehicle and its own insurance. BeavEx and Delivery Express have arrangements to cover gaps, unusual workloads, or urgencies. To ensure continuity, back-up drivers are identified and trained on the routes for familiarity as an additional backstop safety measure. Both vendors have other clients.

For example, BeavEx serves Bank of America, US Bank, Walgreens, and McKesson Drugs. Delivery Express serves University of Washington Medicine, Harborview, Paccar, and Lab-Corp.

During the evaluation process, it was discovered that the vendors treated the application of the federal Private Express Statutes (PES) differently. The PES is a group of laws under which the USPS has the exclusive right, with certain limited exceptions, to carry letters for compensation. The PES is based on the provision in the U.S. Constitution that empowers Congress "to establish Post Offices." These statutes were adopted to reserve to the USPS a sufficient revenue base to enable it to service all areas of the nation equitably, at uniform rates, including areas where services are not self-sustaining. Unless exemptions and exceptions to the PES apply, payment of postage is required even if delivered outside the USPS system. Consequently, the application of the PES can have a significant effect on the price of service.

For example, an individual or company may transport without restriction his or her own letters if it uses its regular salaried employees as couriers. This exemption currently applies to CMS. In contrast, couriers contracted for the same service do not qualify under this exception to the PES. Therefore, postal fees would apply to such mail in addition to the cost of the contract courier.

Another exception to the payment of postage is where the cost of the private courier is at least $3.00 or twice the applicable first-class rate (including priority mail) and the letter will lose its value or usefulness if not delivered within specific urgent time limits. This is the general definition of an extremely urgent letter ("express mail") that can be delivered outside the USPS system without the payment of postage.

DES was advised by the Attorney General's Office that the PES handling and fee structures for express mail would apply to a private carrier with whom the state would contract to handle state mail pickup and delivery. In the proposal process, BeavEx indicated it did not include the effect of the PES in its proposed price because it had many clients with a requirement for same day delivery, and that these clients were not affected by the PES. Delivery Express indicated its proposed price did include the effect of the PES.

The vendors were provided additional information and asked to submit a pricing proposal based on the Attorney General's Office opinion that the PES applied to these services. After receiving the two vendors' responses, both were queried through email, seeking confirmation that the PES was considered in their proposals and that they agreed to reimburse the state for any additional postal cost the state could incur due to the PES. BeavEx indicated it would need much more information about the deliveries and would not agree to the reimbursement. Delivery Express indicated it would agree to this term.

BeavEx proposed serving all seven routes with one route being broken into two separate routes. Delivery Express likewise proposed serving all seven routes. BeavEx provided the lowest annual price.

Vendor	Proposed Total Annual Price
Delivery Express	$1,416,239
BeavEx	$ 509,619

However, BeavEx prices did not include the effect of the PES and would not agree to reimburse the state for any additional cost if BeavEx's cost assumption proved inaccurate. As a result, BeavEx's cost proposal was determined to be nonresponsive.

A DES evaluation team also reviewed the details of each vendor's proposal and attended a vendor presentation to further clarify their proposals. Both vendors scored poorly in their management and technical proposal. Neither provided clear answers to questions about how their programs operated. BeavEx scored 33 out of 50 points. Delivery Express scored 30 out of 50 points.

A. Recommendation

Based upon the scores, the only responsible bidder for which an award could be made is Delivery Express. However, an award cannot be made because the mail delivery outside Thurston County cannot be provided by the private sector at a reduced cost. Therefore, DES is directed to cancel the procurement without entering into a contract.

i. Basis for Recommendation – Cost Savings

In order to compare costs with the private sector vendors, DES converted its direct costs for performing these services into annual total and monthly total price amounts. Direct costs included full-time equivalent employee costs (salary and benefits), vehicle lease amounts, billable miles, fuel and maintenance, cell and data equipment costs. The amounts for each route are outlined in the following chart.

Route Name	Route #	Total Monthly Direct Cost	Total Annual Direct Cost
SODO	9	$5,842	$70,104
SOUTH	10	$8,075	$96,905
NORTH	11	$8,101	$97,215
MONROE	12	$7,792	$93,503
WEST	13	$8,216	$98,588
METRO	14	$5,767	$69,199
TACOMA	15	$5,801	$69,615
Total DES Direct Costs		**$49,594**	**$595,128**

The total annual direct cost for DES to provide the service is $595,128, which is approximately $821,000 lower than Direct Express' proposed price. When including allocations for DES' indirect costs (e.g., human resources, payroll, and accounting support), the total annual cost increases by an estimated $170,000 to $765,128. In this instance, it is not clear the indirect costs could be avoided by a contract to the private sector; those charges would likely be redistributed to the remainder of the CMS division. However, even assuming that indirect costs would be avoided, a contract with Delivery Express would increase state costs by approximately $651,000.

Basis for Recommendation – Efficiencies

Efficiencies were not thoroughly evaluated given the significant cost increase that would result from the procurement. However, there is some indication that current efficiencies would be lost. For example, state agencies frequently pick up a package from one site and deliver it to the next site on the route without additional charge or having to return it to CMS for processing. Delivery Express would not provide that service, but would pick up the package and deliver it to CMS in Olympia for processing and delivery in the same manner as all other mail picked up that day. In this scenario, not only would the state lose the efficiency of quick delivery of such package, charges would apply and state costs would increase.

If you have any questions, please contact Julie Murray, OFM Director of Legal and Legislative Affairs, at (360) 902-0647.

cc: Julie Murray, Office of Financial Management